



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

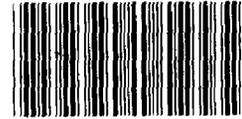
115648
M. S. Fowler

PROCUREMENT, LOGISTICS,
AND READINESS DIVISION

B-202333

JUNE 26, 1981

The Honorable Mark S. Fowler
Chairman, Federal Communications Commission



115648

Dear Mr. Fowler:

Subject: [FCC Did Not Act in the Government's
Best Interest in Acquiring Leased
Space] (PLRD-81-39)

We have completed our review of the five leases for office space which the Federal Communications Commission (FCC) negotiated under its independent leasing authority. Four of those leases provide approximately 64,000 square feet of space at an annual cost of about \$773,000. The remaining lease, which expired in December 1980, provided 6,162 square feet at a total cost of nearly \$64,000.

At the request of the Chairmen, Subcommittee on Public Buildings and Grounds, House Committee on Public Works and Transportation, and the Senate Committee on Environment and Public Works, we reviewed proposed terms and conditions of two additional leases which FCC had planned to enter into for consolidated office space in Rosslyn, Virginia. Those leases would have provided about 375,000 square feet of space at an estimated annual cost of \$6.4 million. (See enc. II.) We reported orally to the House Subcommittee and the Senate Committee on a number of issues concerning the Rosslyn leases. Some of those issues are included in this report.

FCC's independent leasing authority is set to expire in September 1981, pending congressional action on the continuing resolution for FCC's fiscal 1981 appropriation. In addition, following a March 18, 1981, hearing of the House Subcommittee on Public Buildings and Grounds, FCC voted to defer action on Rosslyn or any alternative location for consolidated space until the Senate confirmed your appointment as FCC chairman.

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This report is based on our examination of lease files and related records maintained at FCC headquarters; discussions with the Associate Executive Director (Operations), the contracting officer, and other FCC officials involved in leasing operations; and review of Federal procurement laws, policies, and procedures concerning acquisition of leased space, including the Federal Property and Administrative Services Act of 1949 (40 U.S.C. 471 *et. seq.*), the Economy Act of 1932 (40 U.S.C. 278a), the Federal Procurement Regulations, and implementing directives and guidance issued by the General Services Administration (GSA). Although most Federal Procurement Regulations do not apply specifically to leasing of real property, GSA, as the central authority for leasing general-purpose office space Government-wide, has adopted and implemented many of those regulations in its leasing program to encourage maximum competition and to ensure acquisition of space to the best advantage of the Government.

Our findings, conclusions, and recommendations are summarized below. Detailed information on our findings is provided in enclosure I.

FEDERAL PROCUREMENT POLICIES AND PROCEDURES NOT FOLLOWED

We found several instances in which FCC did not fully follow Federal procurement policies and procedures or did not act in the Government's best interest in exercising its independent leasing authority. Specifically, FCC:

- Did not prepare and issue a formal solicitation for offers for each lease setting forth space requirements and proposed terms and conditions. As a result, there is no assurance that FCC encouraged maximum competition, provided all interested lessors with an opportunity to compete on an equal basis, applied uniform criteria in evaluating alternative proposals, and selected the alternative most advantageous to the Government. (See p. 7.)
- Agreed, or proposed to agree, to escalation of base rent according to a formula tied to annual increases in the Consumer Price Index. This type of escalation is contrary to the GSA and Postal Service policy. These organizations account for about 87 percent of all Federal expenditures for leased space. We recognize that tight leasing markets in Washington, D.C., and other major cities are commanding provisions for rental escalation in commercial leases. However, considering the potential impact of base-rent

escalation on Federal budgetary outlays and leasing costs, we do not believe that FCC should be setting a precedent for the Government on rental escalation. (See p. 9.)

--Did not include certain standard Government lease clauses, such as the Economy Act limitation on annual rent, which GSA uses to implement statutory requirements or to protect the Government's interests. Also, FCC agreed, or proposed to agree, to a provision on arbitration that appears to be inconsistent with a Comptroller General decision. (See p. 10.)

--Did not maintain negotiation memoranda and other standard forms and did not follow procedures prescribed by Federal Procurement Regulations and used by GSA. (See p. 6.)

We believe these deficient practices stemmed primarily from FCC's lack of leasing expertise and its failure to fully and properly use the expertise and advice of its contracting officer. In a September 1980 report, FCC's Internal Review Division recommended that FCC consider strengthening the role, position, and visibility of its contracting officer by placing his function at a higher level within the Office of the Executive Director. Implementing this organizational change may ensure that FCC's contracting officer is fully involved in leasing operations and would prevent the types of deficient practices discussed in this report.

In addition to not following Federal procurement policies and procedures, FCC exceeded its authority by entering into or planning to enter into multiple-year leases contingent solely upon the availability of appropriations. FCC does not have long-term independent leasing authority and has not been delegated such authority by GSA. Its authority to lease is contained in annual appropriation acts (see pp. 5 and 12).

RECOMMENDATIONS

We recommend that the Commission, in any future acquisitions of leased space, follow the Federal procurement policies and procedures which GSA has implemented in its leasing program. This will encourage maximum competition and ensure acquisition of space to the best advantage of the Government. At a minimum, the Commission should:

--Prepare and issue a formal solicitation for offers setting forth space requirements and proposed lease terms and conditions.

--Include in negotiations all standard contract clauses used by GSA to implement statutory requirements or to protect the Government's interests.

--Decline to accept lease provisions permitting annual escalation of base rent unless GSA accepts and implements such practices as standard Government policy.

--Maintain in the lease files memoranda showing price and related negotiation objectives and the rationale for negotiated lease terms and conditions.

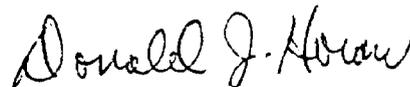
To ensure that these policies and procedures are enforced, we recommend that the FCC contracting officer be fully involved in the leasing process, including solicitation for offers, negotiation of lease terms and rental rates, and contract award and administration.

We also recommend that FCC not exceed its authority by entering into multiple-year leases.

As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget, and the Chairmen, House Committees on Appropriations, on Government Operations, and on Public Works and Transportation; Senate Committees on Governmental Affairs and on Environment and Public Works; and the House and Senate Committees responsible for FCC oversight.

Sincerely yours,



Donald J. Horan
Director

Enclosures - 2

FCC'S LEASING PRACTICES WERE NOT
IN ACCORDANCE WITH FEDERAL
PROCUREMENT POLICIES AND PROCEDURES

BACKGROUND

GSA was created by the Federal Property and Administrative Services Act of 1949 (40 U.S.C. 471 et seq.). The primary purpose for enactment of this law was to centralize in a single Government agency responsibility for the housekeeping functions of the executive branch--procurement, management of real property, records management, and other functions. Among other things, the law authorized the Administrator of General Services to prescribe uniform procurement procedures and to lease general-purpose space Government-wide.

GSA has developed Federal Procurement Regulations which apply to Federal agencies, including FCC. These regulations contain standard lease clauses, such as the Economy Act limitation, failure in performance, and maintenance of premises clauses, which are intended to implement statutory requirements or to protect the Government's interests. Most of the other Federal Procurement Regulations applicable Government-wide are directed to the acquisition of personal property and nonpersonal services and not specifically to the leasing of real property. Nevertheless, GSA has adopted and implemented many of those regulations in its leasing program to encourage maximum competition and to ensure acquisition of space to the best advantage of the Government.

In its Appropriation Act for fiscal year 1980, FCC was granted the authority to lease office space independently of GSA. This authority was extended under a continuing resolution for FCC's fiscal 1981 appropriation and will expire in September 1981. According to the legislative record, FCC was granted independent leasing authority because GSA had not been timely in meeting FCC's space needs.

In addition to space acquired under its independent leasing authority at 2 buildings in Washington, D.C. (see p. 14), FCC occupies about 372,000 square feet in three Washington area buildings under GSA leases having total annual rental costs of about \$2.8 million. The owners of two of these buildings have notified GSA that the leases will not be renewed upon their expirations in 1982.

On February 24, 1981, FCC submitted to the House Subcommittee on Public Buildings and Grounds a prospectus for leasing office space in two towers under construction in Rosslyn, Virginia. According to the prospectus, FCC proposed to enter

into two leases, for terms of up to 20 years, totaling 375,000 square feet at an estimated annual cost of \$6.387 million. (See p. 14.) This space was to be used to consolidate the FCC headquarters offices that are now dispersed among five buildings. FCC believed that, by consolidating in Rosslyn, it would avoid substantial increases in leasing costs resulting from expiration of its current leases and acquisition of replacement space at dispersed locations with significantly higher rental rates.

During a March 18, 1981, hearing on the prospectus, the House Subcommittee raised several objections to FCC's proposed move to Rosslyn. FCC later voted to defer action on Rosslyn or any alternative location for consolidated space until the Senate confirmed a new FCC chairman.

FCC'S CONTRACTING OFFICER WAS NOT INVOLVED IN LEASE NEGOTIATIONS

Federal Procurement Regulations state that the contracting officer has the central role in procurement operations and that the officer always has the responsibility to determine the suitability of contract price (41 CFR 1-3.801-2). Under GSA's leasing procedures, the contracting officer is the focal point for price negotiations and other key steps of the leasing process.

In a September 1980 report which examined certain consultant services contracts, FCC's Internal Review Division stated that, in most cases, the agency's contracting officer had not been informed or made aware of the true circumstances or background of the contracts he was asked to sign on behalf of the Government. The report noted that preliminary negotiations or searches for prospective contractors were undertaken before the contracting officer was advised that a contract was being negotiated. The most glaring of the deficiencies in this regard was the total lack of inclusion of the contracting officer in the negotiation of price. To correct these conditions, Internal Review recommended that FCC consider strengthening the role, position, and visibility of the contracting officer by placing his function at a higher level within the Office of the Executive Director. This action, according to Internal Review, would tend to strengthen the hand of the contracting officer in direct dealings on contractual matters with the heads of FCC bureaus and offices.

In our review of FCC's signed and proposed leases, we found the same conditions as reported by the Internal Review Division. Lease negotiations were handled primarily by the Associate Executive Director (Operations) and an outside realty consultant. The contracting officer, who is subordinate to the

Associate Executive Director, had little or no involvement in lease negotiations and determinations of price. Only limited records showing the rationale for negotiated lease terms and conditions were available. For example, negotiation memoranda spelling out FCC's price and related bargaining objectives, exceptions to its proposed terms and conditions, and the results of negotiations with lessors were not maintained in the lease files. Such memoranda are required by Federal Procurement Regulations (41 CFR 1-3.811) and GSA leasing procedures. Furthermore, a formal solicitation for offers was not prepared for each of the leases and certain standard clauses and provisions prescribed by Federal Procurement Regulations or used by GSA were omitted from some of FCC's leases (see pp. 7 and 10).

These deficiencies may have been avoided if FCC had fully involved its contracting officer in the leasing process and had abided by his advice to follow established GSA leasing guidelines. In a September 1980 memorandum to the chief of the Operations Support Division, the contracting officer stated that:

"Where statutory matters are concerned I believe we should utilize any GSA directive, as a guide, that implements a public law * * * [an example is] a GSA directive that implements the Economy Act provisions * * *. I also believe that the provisions of the Federal Property and Administrative Services Act of 1949 * * * apply to our space acquisition transactions and its implementation * * * should be adhered to, especially if we can have the benefit of that implementation in the guidance of a GSA directive * * *."

Also, the contracting officer stated that, in his view, it was imperative that extraordinary effort be taken to document all lease actions.

According to an agency official, FCC had intended to comply with all statutory requirements in acquiring leased space. However, because its space needs were urgent, FCC did not feel obliged to follow the leasing policies and procedures used by GSA. We believe that FCC should have followed Federal Procurement Regulations and GSA's leasing guidelines, since we perceive no sound reason why the principles inherent in the competitive procurement system should not be applied to lease activities. Furthermore, they are intended to ensure acquisition of leased space to the best advantage of the Government.

FCC DID NOT USE FORMAL
SOLICITATIONS FOR OFFERS

Generally, leased space is acquired by negotiation rather than by advertised sealed bids because true competition--in the

sense that bidders are offering the same or substantially the same property--is impossible since no two buildings are alike. Federal Procurement Regulations require that, whenever property or services are to be procured by negotiation, proposals shall be solicited from the maximum number of qualified sources (41 CFR 1-3.101). As we stated in our January 24, 1978, report (LCD-77-354), offering all qualified individuals an opportunity to compete provides greater assurance that acceptable space is obtained at the most economical rental.

GSA's leases are negotiated procurements. Its policy requires that competition be obtained to the maximum extent practical among suitable and available locations meeting minimum Government standards. To ensure that competing offers are proposed, compared, and evaluated on the basis of uniform criteria, GSA prepares and issues a formal solicitation for offers specifying its space requirements and proposed lease terms and conditions. This solicitation is the basis of the entire process of negotiation. Offers received in response to the solicitation must be evaluated in strict accordance with its provisions.

FCC did not prepare, issue, and conduct negotiations on the basis of a formal solicitation setting forth its space requirements and proposed terms and conditions for each of its leases. Instead, FCC initiated sole-source negotiations on the basis of the locations identified by its realty consultant. As a result, there is no assurance that FCC encouraged maximum competition, provided all interested lessors with an opportunity to compete on an equal basis, and acquired leased space to the best advantage of the Government.

The effect of not using a formal solicitation was most apparent in the case of the proposed Rosslyn leases. In December 1980, FCC considered a proposal to put the leases into effect but voted instead to determine whether alternative space was available. A realty ad was placed in a local newspaper which specified only that the space total approximately 425,000 square feet, be readily accessible by public transportation, have adequate parking facilities, be made available before June 30, 1983, and be located within the District of Columbia. Several responses were received, but since the offerors had based their proposals on limited information, it was impossible to fully compare and evaluate rental rates and other terms or to conclude which alternative (including Rosslyn) was the most advantageous. For example, the Rosslyn leases included unique provisions for escalation of base rent which could have resulted in annual rental payments substantially higher than the \$6.387 million estimated by FCC. Without detailed information on the escalation provisions proposed by other offerors, it is impossible to determine which proposal is the most economical.

Furthermore, because the proposed terms and conditions of the Rosslyn leases had become generally known, at least one offeror used those leases as a basis for a proposal. This circumstance, in which one offeror has knowledge of a competitor's pricing information, can lead to the auctioning of offers against one another. Since auctioning is prohibited by Federal Procurement Regulations (41 CFR 1-3.805-1), GSA forbids public disclosure of offerors' proposals.

FCC'S RENTAL ESCALATION PROVISIONS
ARE CONTRARY TO FEDERAL POLICY

GSA and the Postal Service, which account for about 87 percent of all Federal expenditures for leased space, do not permit annual escalation of net rent (gross rent less operating expenses and real estate taxes), although they do allow for escalation or pass-throughs of annual increases in operating expenses and taxes. In two of its signed leases and both of its proposed Rosslyn leases, FCC agreed to annual escalation of base rent (net rent plus services and taxes), in addition to annual escalation or pass-throughs of increased operating expenses and taxes. Furthermore, although GSA leases explicitly provide that the Government will benefit from decreases in real estate taxes, four of the six FCC leases permitting pass-through of tax increases did not contain this benefit.

Annual escalation of net or base rent can substantially increase budgetary outlays over the term of a lease. For example, on the basis of FCC's prospectus for the Rosslyn leases, the budgetary outlay over a 20-year period would have totaled about \$121 million, excluding base-rent escalation. ^{1/} According to the proposed leases, base rent would have been escalated according to a formula tied to annual increases in the Consumer

^{1/}FCC's estimated annual cost of the Rosslyn leases was \$6.387 million, excluding base-rent escalation. Projecting this figure over a 20-year period, we estimate the total outlays would have amounted to \$127.74 million, assuming that the Rosslyn space were fully occupied throughout the lease term. However, FCC had planned to occupy the space in stages between the fall of 1981 and spring of 1983 and thus would not have paid the full \$6.387 million in every lease year. Our estimated total outlay of \$121 million reflects FCC's planned occupancy schedule.

Price Index (CPI). 1/ Assuming a 5-percent annual increase in the CPI, we estimate that the total outlay would have increased by about \$49 million, or 40 percent, to \$170 million for the entire lease term. Assuming a 10-percent annual increase, the total outlay would have more than doubled to about \$244 million. These estimates reflect only base-rent escalation and do not include additional outlays that would have resulted from annual escalation or pass-throughs for increased operating expenses and taxes.

Because demand is high and available office space is limited in Washington, D.C., and other major cities, commercial lessees are agreeing to pay rental escalation. However, FCC did not fully analyze and project the impact of base-rent escalation on budgetary outlays and lease costs. Considering the potential size of that impact and its implications for Federal leasing, we do not believe that FCC should be setting a precedent for the Government on rental escalation.

FCC OMITTED STANDARD CONTRACT
CLAUSES AND ACCEPTED LEASE PROVISIONS
INCONSISTENT WITH FEDERAL POLICY

In one or more of its signed or proposed leases, FCC either

- did not include certain standard Government clauses, such as the Economy Act limitation on annual rent, which GSA uses to implement statutory requirements or to protect the Government's interests;
- included the Economy Act clause but did not include the standard GSA lease provision which prevents the act's rental limitation from being exceeded as a result of annual passthroughs for real estate tax increases; or
- included a provision on arbitration that appears to be inconsistent with a Comptroller General decision.

1/The leases would not, however, have permitted FCC to benefit commensurately from any decreases in the CPI. According to an FCC official, base-rent escalation was included to protect the lessor's equity in the property against inflation. However, some equity protection is already afforded by inflationary increases in the property's market value.

Economy Act limitation
on annual rent

Section 322 of the Economy Act of 1932 (40 U.S.C. 278a) generally limits the annual rental that the Government may pay to no more than 15 percent of the appraised fair market value of the property at the date of the lease. To implement this statutory limitation, GSA includes in its leases a standard Economy Act clause and a provision which prevents the 15-percent ceiling from being exceeded as a result of annual pass-throughs for increases in real estate taxes.

One of the five leases signed by FCC did not include the Economy Act clause. Of the remaining four leases, two permitting annual pass-throughs for taxes did not include the GSA provision that prevents the 15-percent ceiling from being exceeded. This provision also was omitted from the proposed Rosslyn leases, although the base-rent escalation contained in those leases quite likely would have resulted in annual rent increasing to a level higher than the 15-percent ceiling several years before lease expiration.

In discussions with us, FCC officials appeared to believe that the fair market value of leased property could be reappraised during the lease term. According to the act, however, the 15-percent limitation applies to fair market value at the date of the lease. If real property could be reappraised when convenient during the lease term to avoid the 15-percent ceiling on annual rent, the Economy Act limitation would be meaningless.

Other standard contract clauses

In addition to the Economy Act clause, FCC omitted from one of its signed leases the following standard Government clauses prescribed by Federal Procurement Regulations and used by GSA:

- Failure in performance - Gives the Government the right to deduct from rental payments the costs of any service, utility, maintenance, or repairs which the lease requires but the lessor fails to provide.
- Maintenance of premises - Requires the lessor to maintain the premises in good repair and tenantable condition, except in case of damage arising from the act or negligence of the Government's agents or employees.
- Alterations - Gives the Government the right to make alterations, attach fixtures, and erect structures or signs in or upon the leased premises and retains for the Government ownership control over such fixtures, additions, or structures.

--Damage by fire or other casualty - Gives the Government the right to terminate the lease in the event the leased premises are destroyed or rendered untenable by fire or other casualty.

--Subletting the premises - Gives the Government the right to sublet any part of the premises it leases.

Omission of these clauses appeared to stem directly from FCC's inexperience with leasing. FCC officials attempted to include the clauses shortly before the lease was signed, but the lessor refused on the grounds that he never would have begun negotiations if he had known the clauses would be included. In a subsequent memorandum, FCC's Office of General Counsel reluctantly approved the lease, but advised that prospective lessors should be made aware that the standard Government clauses are a negotiation guide which cannot be ignored or bargained away.

Arbitration provision

In a 1953 decision (32 Comp. Gen. 333) and in subsequent opinions, the Comptroller General has held that, in the absence of specific statutory authority, a Government agent generally is not free to submit to arbitration those controversies to which the United States is a party and which have the effect of imposing additional obligations on the Government.

Two of the leases signed by FCC contain a provision for arbitration if the CPI is discontinued without a successor and if the parties cannot agree on a substitute index. A similar provision was included in the proposed Rosslyn leases. Since the CPI is used to escalate FCC's rental payments, a substitute index determined by arbitration could result in additional obligations to the Government. While we recognize that likelihood of having to arbitrate a substitute index is quite remote, the arbitration provision contained in the FCC leases appears to be inconsistent with the Comptroller General decision.

MULTIPLE-YEAR LEASING AUTHORITY

FCC has entered into or planned to enter into multiple-year leases for space whose continuance from year to year would be contingent solely upon the availability of appropriations. FCC does not independently possess long-term leasing authority and has not been delegated such authority by GSA. Furthermore, FCC's appropriations provide obligation authority for leasing only on a fiscal year basis. Under these circumstances, the entering into long-term leases whose continuance from year to year is contingent solely

upon the availability of appropriations is a violation of the Anti-deficiency Act, 31 U.S.C. § 665. See Leiter v. United States, 271 U.S. 204 (1926); Goodyear Tire and Rubber Company v. United States, 276 U.S. 287 (1928); 48 Comp. Gen. 497, 501; 20 Comp. Gen. 30 (1940); and B-88974, November 10, 1948. However, where the lease requires an affirmative act by the Government to continue it beyond the end of the fiscal year (for example, the exercise of an option to renew) is not a violation of the law.

Thus, unless FCC obtains long-term leasing authority either by delegation from GSA or by enactment of legislation by the Congress, it should include in its leases a clause requiring an affirmative action by an FCC officer to continue the lease beyond the end of the fiscal year.

LEASES SIGNED OR PROPOSED BY FCC
UNDER ITS INDEPENDENT LEASING AUTHORITY

<u>Location</u>	<u>Term of lease</u>	<u>Annual rent</u>	<u>Square footage</u>	<u>Annual cost per sq. ft.</u>
Washington, D.C.:				
2555 M St., NW. (1st and 2d floors)	1/03/80 to 6/29/81	\$132,169	7,578	\$17.43
2000 L St., NW. (2d floor)	9/01/80 to 8/31/85	<u>a/b</u> /305,130	21,795	14.00
2000 L St., NW. (8th floor)	9/01/80 to 8/81/85	<u>a/b</u> /16,156	5,068	17.00
2033 M St., NW. (2d floor)	3/10/80 to 12/14/80	<u>c</u> /63,777	6,162	13.50
Gettysburg, Pa.	6/81 to 6/91	<u>a</u> /249,139	29,345	8.49
Rosslyn, Va.	Up to 20 years, beginning in fall 1981	<u>a/b</u> /6.387 million (est.)	375,000	17.03 (est.)

a/Plus annual escalation or pass-through for increases in operating expenses and real estate taxes.

b/Plus annual escalation of base rent linked to increases in the Consumer Price Index.

c/Full cost of expired lease.